30 November 2012

Dear Sirs

Comprehensive review of the IFRS for SMEs

We appreciate the opportunity to comment on the Request for Information – Comprehensive Review of the IFRS for SMEs (‘RFI’). We have consulted within the KPMG network in respect of this letter, which represents the views of the KPMG network.

We support the International Accounting Standard Board’s (‘IASB’) initiative to undertake a comprehensive review of the IFRS for SMEs (‘the Standard’) after two years of practical experience in dealing with the Standard by a broad range of entities around the world. We agree with the IASB’s approach of issuing the RFI to solicit views of interested parties before proposing actual amendments to the Standard.

Overall, we believe that the IASB should continue to preserve the stand-alone and simplified nature of the Standard by limiting accounting policy options and eliminating any fallback to full IFRS. While we favour the continued alignment of the Standard with the requirements in full IFRS, we are concerned that the requirements of IFRSs 10 and 11 are complex and judgemental to apply for SMEs. We therefore would strongly recommend that these requirements should be simplified significantly when they are incorporated into the Standard, so as not to compromise the aim of providing a simple set of accounting principles that are appropriate for the circumstances of SMEs.

We have set out our detailed responses to the questions in the RFI in the appendix to this letter.

Please contact Mark Vaessen or Jim Tang at +44 (0) 20 7694 8871 if you wish to discuss any of the issues raised in this letter.

Yours faithfully

KPMG IFRG Limited

cc. Hans Hoogervorst, Chairman of the IASB
cc. Ian Mackintosh, Vice Chairman of the IASB
cc. Paul Pacter, Chairman of the SMEIG
cc. Haydeé de Chau, member of the SMEIG
Appendix

Part A – Response to specific questions

S1. Use by publicly traded entities (Section 1) – Are the scope requirements of the IFRS for SMEs currently too restrictive for publicly traded entities?

Response: a

With respect to the scope of the Standard, notwithstanding our response to S2 and S3, we believe that generally publicly traded entities have significant public accountability and the simplified disclosure requirements in the Standard are not suitable for these entities.

S2. Use by financial institutions (Section 1) – Are the scope requirements of the IFRS for SMEs currently too restrictive for financial institutions and similar entities?

Response: c

In general, with respect to scope of the Standard, we agree with the view that governments and regulatory authorities in each individual jurisdiction should decide which entities may apply the Standard within their respective jurisdictions. This is especially relevant for financial institutions given the differing nature and complexity of such entities around the world.

We believe that this is consistent with the IASB’s observation in paragraph P10 of the Standard, which states that many jurisdictions around the world have developed their own definition of SMEs for a broad range of purposes including prescribing financial reporting obligations.

We note that, however, the term ‘financial institutions’ encompasses a wide spectrum of entities of differing complexity and public accountability; we therefore believe that the further explanation about the objectives and limitations of the Standard, in particular why the Standard is not suitable for users of the financial statements of certain entities, would help governments and regulatory authorities in different jurisdictions decide the appropriate scope.

Further, if the jurisdiction in which an entity operates does not have any specific requirement on the scope of the Standard, then we suggest that the scope as suggested in Section 1 of the Standard (and amended as appropriate, see response to S3 below) should apply.

S3. Clarification of use by not-for-profit entities (Section 1) – Should the IFRS for SMEs be revised to clarify whether a not-for-profit (NFP) entity is eligible to use it?

Response: d

As stated in response to S2, we believe that the governments and regulatory authorities in each individual jurisdiction should decide which entities may apply the Standard within their respective jurisdictions.

Notwithstanding the above, Paragraph 1.3 of the Standard states that an entity has public accountability if, among other things, it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. We believe that the phrase ‘holds assets in a fiduciary
capacity’ is unclear: while we agree that entities such as large banks that hold assets from a broad group of customers as creditors should generally be precluded from applying the Standard, we believe that a different consideration applies to NFP entities that do not have an obligation to repay the assets donated by third parties but are responsible for using these assets in manner consistent with their objectives and any agreed constraints. In our view, merely accepting contributions would not, by itself make a NFP entity publicly accountable and the Standard should remain flexible in this regard.

If the meaning of ‘holding assets in a fiduciary capacity’ was extended to cover all instances where an entity holds assets contributed by a broad group of outsiders, then we are concerned that this might lead to unintended widening of the scope exclusions of the Standard. For example, do entities that provide key infrastructure and whose operations are very material to the local economy have public accountability for the purposes of the Standard?

In view of the above, we recommend that the meaning of fiduciary capacity should be clarified and tightened in the Standard.

**S4. Consideration of recent changes to the consolidation guidance in full IFRS (Section 9)**

Should the changes to full IFRS introduced by IFRS 10 *Consolidated Financial Statements* be reflected in the IFRS for SMEs, but modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations?

Response: c

We agree that aligning the Standard with the requirements in IFRS 10 would not affect most straight-forward parent-subsidiary relationships. However, we believe that the requirements of IFRS 10 would be complex and would involve significant judgement in its application for borderline cases.

Therefore, while we believe that the requirements in the IFRS for SMEs should remain aligned with full IFRS in principle, we strongly recommend that the requirements of IFRS 10 should be significantly simplified when incorporated into the Standard, in line with the aim of providing a simple set of accounting principles that are appropriate for the circumstances of SMEs.

**S5. Use of recognition and measurement provisions in full IFRS for financial instruments (Section 11)**

How should the current option to use IAS 39 *Financial Instruments: Recognition and Measurement* in the IFRS for SMEs be updated once IFRS 9 *Financial Instruments* has become effective?

Response: c

As indicated in the objective and paragraphs BC81-BC88 of the Standard, the IASB intends the Standard to be a stand-alone document, and the current option to apply IAS 39 is the only fallback to full IFRS in the Standard.

We are of the view that, consistent with the IASB’s objective as stated above, the option to fall back to IAS 39 should not be continued in the Standard, and that the requirements of IAS 39 or
IFRS 9 should be incorporated in the Standard and modified as appropriate to take into account users’ needs and cost-benefit considerations. We believe that the Board’s reasons for including the fallback option as outlined in paragraph BC106 of the Standard can be addressed by incorporating the relevant requirements from full IFRS in the Standard after appropriate modifications. This will fully meet the objective of the Standard to be a stand-alone document.

S6. Guidance on fair value measurement for financial and non-financial items (Section 11 and other sections) – Should the fair value guidance in Section 11 be expanded to reflect the principles in IFRS 13 Fair Value Measurement, modified as appropriate to reflect the needs of users of SME financial statements and the specific circumstances of SMEs (for example, it would take into account their often more limited access to markets, valuation expertise, and other cost-benefit considerations)?

Response: b

We believe that the fair value guidance in the Standard should be updated to align with the requirements of IFRS 13, with appropriate modifications to balance user needs and cost benefit considerations.

Although IFRS 13 does not require any new fair value measurements under full IFRS, it does establish a framework for measuring fair value for financial and non-financial assets and liabilities. We believe that IFRS for SMEs would benefit from a similar comprehensive framework for fair value measurement.

In relation to disclosures, IFRS 13 provides a comprehensive disclosure framework. While we believe that some of the disclosure are useful in understanding the measurement of assets and liabilities, care should be taken to introduce additional disclosure requirements only after due consideration of costs and benefits. For example, while providing reconciliation from opening balances to closing balances under paragraph 93(e) of IFRS 13 could be relatively simple to provide and useful for users, sensitivity disclosures under paragraph 93(h) of IFRS 13 might be challenging for some preparers.

S7. Positioning of fair value guidance in the Standard (Section 11) – Should the guidance be moved into a separate section?

Response: b

We believe that including all guidance on fair value measurement and disclosures in a separate section of the Standard will reduce complexity and improve consistency in application, thereby enhancing the comparability of information reported in financial statements.
S8. Consideration of recent changes to accounting for joint ventures in full IFRS (Section 15) – Should the changes to joint venture accounting in full IFRS introduced by IFRS 11 Joint Arrangements be reflected in the IFRS for SMEs, modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations?

Response: c

We are aware that applying IFRS 11 requirements involves significant judgement, especially where a SME is involved in more complex joint arrangements. Thus, similar to our response to S4, while we support alignment, we believe that significant simplifications should be made to take into account the circumstances of SMEs.

S9. Revaluation of property, plant and equipment (Section 17) – Should an option to use the revaluation model for property, plant and equipment be added to the IFRS for SMEs?

Response: b

While we generally hold the view that allowing an accounting policy choice in the IFRS for SMEs could result in significant non-comparability, we understand that there is a genuine user need for the revalued amount of a SME’s property, plant and equipment. For example, some SMEs may need to recognise the revalued amount of their property, plant and equipment in their financial statements when obtaining loans. Therefore, we support the introduction of an accounting policy option to use the revaluation model for property, plant and equipment.

S10. Capitalisation of development costs (Section 18) – Should the IFRS for SMEs be changed to require capitalisation of development costs meeting criteria for capitalisation (on the basis of on the criteria in IAS 38 Intangible Assets)?

Response: a

We do not support the introduction of a requirement to capitalise development costs. We agree with the IASB’s original rationale, as set out in paragraph BC113 of the Standard, that a requirement to capitalise development costs would involve costs that are outweighed by the benefits. In addition, we believe that introducing the requirement would introduce complexity into the IFRS for SMEs.
S11. Amortisation period for goodwill and other intangible assets (Section 18) – Should paragraph 18.20 be modified to state: “If an entity is unable to make a reliable estimate of the useful life of an intangible asset, the life shall be presumed to be ten years unless a shorter period can be justified”? 

Response: c 

We agree that there could be situations where SMEs are unable to reliably ascertain the life of an intangible asset, but believe that it would be considerably shorter than 10 years. Therefore, we agree with the proposal to introduce a rebuttable presumption. 

However, we recommend that the IASB should clarify whether the rebuttal is mandatory or optional. In particular, if the rebuttal would be mandatory, then we recommend that the IASB should further consider whether the bar ‘unless a shorter period can be justified’ is high and objective enough so as not to defeat the purpose of simplifying the requirements with the rebuttable presumption.

S12. Consideration of changes to accounting for business combinations in full IFRS (Section 19) – Should Section 19 be amended to incorporate the changes introduced by IFRS 3 (2008) Business Combinations, modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations? 

Response: b 

We support aligning the Standard with the requirements under full IFRS with appropriate modifications. In particular, we are aware that there could be some complex areas in IFRS 3 (2008), for example fair value measurement of contingent consideration, which could involve significant judgement and therefore simplification may be appropriate.

S13. Presentation of share subscriptions receivable (Section 22) – Should paragraph 22.7(a) be amended either to permit or require the presentation of the receivable for issue of equity instrument as an asset? 

Response: b 

We believe that share subscriptions receivable and similar receivables should be recognised as assets, if they meet the definition of a (financial) asset. In our view, the Standard should require as opposed to permit this accounting treatment.
S14. Capitalisation of borrowing costs on qualifying assets (Section 25) – Should Section 25 of the IFRS for SMEs be changed so that SMEs are required to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset, with all other borrowing costs recognised as an expense when incurred?

Response: a

We believe that the current requirement to expense borrowing costs should continue for the same reasons as set out in response to S10.

S15. Presentation of actuarial gains or losses (Section 28) – Should the option to recognise actuarial gains and losses in profit or loss be removed from paragraph 28.24?

Response: b

We support the removal of the option as this would further simplify the Standard and improve comparability of financial statements prepared using the Standard. In addition, it will align the Standard with the requirements in revised IAS 19 Employee Benefits.

S16. Approach for accounting for deferred income taxes (Section 29) – Should SMEs recognise deferred income taxes and, if so, how should they be recognised?

Response: a

We believe that the guidance in the IFRS for SMEs for deferred taxes should be aligned to full IFRS. Accordingly, we believe that deferred taxes should be computed by SMEs using the temporary difference approach in accordance with IAS 12 Income Taxes.

S17. Consideration of IAS 12 exemptions from recognising deferred taxes and other differences under IAS 12 (Section 29) – Should Section 29 be revised to conform it to IAS 12, modified as appropriate to reflect the needs of the users of SME financial statements?

Response: b

As stated in response to S16, we believe that the requirements in the Standard should be aligned to the current requirements in IAS 12, with appropriate modifications. In our view, changes, as deemed appropriate, should be made as part of the IASB’s plan on amending the Standard (see response to G1) once the IASB has completed its project on income taxes under full IFRS.
S18. Rebuttable presumption that investment property at fair value is recovered through sale (Section 29) – Should Section 29 be revised to incorporate the exemption for investment property at fair value in paragraph 29.20?

Response: b

We support the inclusion of the exemption. We believe that this would better align the Standard with full IFRS and would also simplify an area of accounting which is particularly challenging and subjective.

Part B – Response to general questions

G1. Consideration of minor improvements to full IFRS - How should the IASB deal with minor improvements to full IFRS such as changes arising out of the annual improvements project, where the IFRS for SMEs is based on old wording from full IFRS?

Response: c

We believe that the IASB should balance the need for keeping the IFRS for SMEs aligned with full IFRS on one hand, and the need to maintain a stable platform for SMEs and to improve the IFRS for SMEs in a cost-effective manner on the other. On balance, we believe that introducing an annual improvements process to the IFRS for SMEs might result in SMEs having to spend additional resources tracking changes to the Standard, with limited benefits. We therefore recommend that the IASB should develop criteria for assessing whether or not to incorporate minor improvements arising from the annual improvements to full IFRS approximately once every three years, in line with the plan as set out in paragraph P17 of the Standard.

G2. Further need for Q&As – Do you believe that the current, limited programme for developing Q&As should continue after this comprehensive review is completed?

Response: a

As stated in our comment letters to draft Q&As (submitted on 14 September 2011, 29 November 2011 and 27 January 2012), we are concerned that the initiative to provide non-mandatory implementation guidance on the IFRS for SMEs, while well intentioned, is inconsistent with the objective of having a single, stable, stand-alone standard for SMEs. We therefore do not recommend the continuance of the Q&A programme.

G3. Treatment of existing Q&As – Should the Q&As already issued be incorporated into the IFRS for SMEs?

Response: a

As stated above in response to G2, we believe that there should not be any parallel non-mandatory guidance on the IFRS for SMEs. Therefore, we recommend that all the existing Q&As should be incorporated into the Standard or the educational materials as appropriate.